



Group 17



EASTWEST INSTITUTE

# Economic Review

## Political Economy of Dictatorship

The peculiarity of dictatorships is that they are transitory political regimes. This does not mean that they are short-lived. Since I have lived most of my life under one type of dictatorship, I am aware that such a regime can last quite long. However, everyone else has also been aware of its transitory character, which is the case with any other dictatorship. As soon as it appears and settles down, it turns from a solution into a problem. This fact determines the content of every study dealing with dictatorships. It has to explain how it is established, how it lasts and it has to anticipate the way it will end.

The first question is why is force used? It is clear that dictatorship is impossible without the use of force. Furthermore, it cannot even be established unless some (possibly massive) force is used and cannot be maintained without permanent reliance on coercion. Nevertheless, to opt for violence instead of other means, one of two conditions has to be fulfilled. Either that force is considered more efficient than other alternatives for achieving the set goal, or that no other instruments are available.

The current reliance on sheer force in Serbia is for the lack of any other alternatives. It is the only instrument left to the government. If possible alternatives are surveyed, that becomes obvious. The usual substitute for force is money or economic opportunities in general. Looking at the resources available to the Serbian government, it is evident that the state is broke - not only in terms of its budget. Much more important is the economic perspective. What opportunities for employment, advancement and development can the Serbian government offer? Apart from a few exceptions, the majority of people in Serbia can expect to face the problems of keeping their jobs, while they can neither hope for promotion, nor for better income and life in a prosperous country. Thus, the present government is unable to offer any economic benefits in exchange for political support.

If there is no money or prospects for improvement, there may exist political instruments for the mobilization of public support. In other words, the state may be bankrupted, but it can still be popular, for one reason or another. The history of hitherto populism in Serbia is quite instructive in that respect. Undoubtedly, the current

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#### Yugoslavia in the Mirror of Eastern Europe - Romania

FRY	1999	1999	IV 2000	IV 2000	IV 2000	I-IV 2000
Basic Economic Indicators		1998		III 2000	IV 1999	I-IV 1999
GDP - USD million	14,224a)	-19.3%	...	...	...	...
Montenegro	...	...	...	...	...	...
Serbia	...	...	...	...	...	...
GDP per capita - USD	1,699a)	-19.1%	...	...	...	...
Montenegro	...	...	...	...	...	...
Serbia	...	...	...	...	...	...
Central Serbia	...	...	...	...	...	...
Vojvodina	...	...	...	...	...	...
Industrial Production	...	-24.1%	...	-10.9%	44.7%	3.4%
Montenegro	...	-7.6%	...	-8.2%	1.7%	-1.6%
Serbia	...	-25.6%	...	-11.0%	48.8%	4.0%
Central Serbia	...	-24.5%	...	-11.1%	52.1%	7.9%
Vojvodina	...	-28.2%	...	-10.8%	41.6%	-4.3%
Average Wage - DM	107	-31.7%	...	...	...	...
Montenegro	154	-14.1%	185	2.2%	21.6%	3.9%
Serbia	102	-33.8%	88	7.4%	-16.9%	-33.8%
Unemployment Rate	27.3%	8.3%	...	...	...	...
Montenegro	36.8%	7.9%	...	...	...	...
Serbia	26.5%	8.2%	...	...	...	...
Export - USD million	1,498	-46.9%	120	-22.8%	47.1%	-8.8%
Montenegro	123	-4.7%	7.3	-66.9%	-36.5%	37.4%
Serbia	1,375	-48.9%	112	-15.6%	60.8%	-12.5%
Import - USD million	3,296	-30.3%	265	-28.4%	76.6%	13.8%
Montenegro	358	6.9%	28	-33.7%	-47.2%	-17.7%
Serbia	2,938	-33.2%	237	-27.7%	143.7%	18.6%
Monetary supply (M1), end of period, DIN billion	16.4	51.9%	17.8	0.8%	48.3%	50.4%
Cash	6.7	34.0%	6.4	4.9%	19.3%	25.8%
Deposits	9.7	67.2%	11.4	-1.7%	71.8%	68.7%
Real money supply, end of period, DM million	739	-42.3%	666	-0.8%	-39.5%	-42.6%
Market exchange rate, monthly level	4.25%	-38.8%	5.12%	-2.8%	134.9%	-17.0%
Retail prices	...	42.4%	...	3.6%	55.3%	53.6%
Montenegro	...	60.1%	...	5.2%	130.6%	130.9%
Serbia	...	41.1%	...	3.5%	50.6%	48.8%
Cost of living	...	44.9%	...	3.6%	62.1%	61.1%
Montenegro	...	67.2%	...	7.2%	140.6%	143.1%
Serbia	...	43.5%	...	3.3%	56.4%	54.9%
Industrial prices	...	44.2%	...	3.7%	93.5%	79.6%
Montenegro	...	63.7%	...	4.0%	137.4%	135.7%
Serbia	...	43.2%	...	3.6%	90.7%	76.2%
Black market exchange rate (din/DM)	12.6	88.1%	23.0	2.2%	114.8%	135.1%

a) G17 estimate based on official information from the Federal Statistics Office

**When one loses popularity, the value of force rises**

**Nationalism becomes an ideology of self-isolation and barriers to growth**

**A threat is only effective if there is fear**

**The key problem of the dictatorship in Serbia is that it cannot become anything else**

regime, which has been in power for over a decade now, not only failed to improve the economic and political position of citizens, but it has indeed been ruling over a period of almost unprecedented decline. This decline has been comprehensive. There is no need to detail various indicators of decline as they are widely known. Nevertheless, the government has managed to preserve at least some of its appeal.

By all measures, there is not much support left now. The lesser the popularity, the larger the use of force. There is something paradoxical in the way this has been happening in Serbia. With the war in Kosovo and the post-war political behavior of both the ruling and opposition parties, the political space has changed significantly. The key change is a waning of the importance and influence of the opposition parties. Because of that, the ruling parties are losing their potential partner. In this way, the usual political resources are lost. Given that economic resources have also been exhausted, to put it mildly, other instruments of mobilization have to be found.

One possible instrument remaining is ideology. Again, the history of the use of ideology in Serbia is more than instructive. Similar to communist methods, the nationalists have succeeded in reducing ideological competition to a space where they have the advantage. If one looks at political polemics in the last ten years, they mostly focus on the issue of genuine nationalism. This is exactly parallel to debates on true Marxism in the former system, which were so intellectually fruitless and politically debilitating. Though nationalism is still the predominant language of political discussions in Serbia, the regime can no longer rely on it for gaining support as it used to do before. The reason is very simple, though it was not easy to explain to so many people ten years ago. Namely, nationalism is an aggressive ideology. Its efficiency depends on its ability to simultaneously include and exclude citizens. As long as those included can beat those not included, it has some power. As soon as there is nobody to hit with nationalist rhetoric, ideology loses its influence. If there are no more territories to conquer, nobody to discriminate, no superior and inferior races, nationalism becomes just an ideology of self-isolation and a barrier to development.

### ***Efficiency of force***

Once economic, political and ideological resources are exhausted, force is the only instrument that remains. There are no secrets about how it works. The ideal of every dictatorship is that the use of threat will be sufficient and that open coercion will not be needed. However, one should take into account the economics of force. Threat is efficient only if the population has accumulated the appropriate level of fear. Then the real use of force can be minimized and the threat of the use of violence will be sufficient. Here, one has to quarrel a little with Thomas Hobbes, who appeared to have argued that fear was inborn in every individual and thus the government did not have to work on the supply of fear. But, the history of dictatorships contradicts that claim. In order for people to fear the government, the government has to credibly threaten the people. Nothing can be more credible than the actual use of force. Hence dictators cannot rely on threats alone. They have to install enough fear into their citizens by coercing them and subjecting them to the open use of force. The display of force has to be ruthless, transparent, drastic and immoral and it has to be just right. Too much or too little coercion may prove to be fatal to the regime.

That is how the current use of force in Serbia can be explained. The regime does not have any other resources to count on. Economic resources are scarce and will not grow. Political resources are depleted, ideological resources are inefficient, so only force remains. No other instrument can give legitimacy to the regime. Only open dictatorship will do the trick. That is the political direction in Serbia.

A dictatorship is not a simple political regime. Yet, in the end it boils down to the relationship between the dictator and the people. In a more or less pure dictatorship, political parties lose their importance and the reliance on force brings the regime in direct contact with the people. So as not to end up losing in this relationship, the use of force has to be carefully devised. The strategy is rather simple. Force has to be used selectively and has to lead to the moral corruption of the people.

Clearly, the legitimization of violence has to be carried out gradually. In certain cases, pure terror can be and has been used. But this is not so immanent to dictatorships. More often, they are maintained by gradual moral corruption of people through the selective use of force. Again, the efficient strategy is very simple. Force is first used against those who have only limited moral support in the community. In Serbia, those were the so-called traitors. Once the population is convinced that these people have no moral rights, the community takes the road of moral degradation.

The next category will be closer to home and then closer and closer, until the people are morally collapsed. In that process, various methods of discrimination may be used. If it is not enough to label somebody as a traitor, then he will be called a terrorist. If that is not enough other categories will be invented. These labels are necessary simply to provide for the justification of the assertion that some people, whoever they might be, do not deserve moral support as they have no moral rights. Once people accept that there are some people who have no moral rights, coercion has succeeded. The necessary amount of fear has been installed in the population and threats, together with the occasional use of force, will be enough afterwards. This is how dictatorship in Serbia will have to be preserved.

### ***The end of coercive regimes***

How will this dictatorship end? The length of every dictatorship is coextensive with the power of the dictator. Ideally, the dictator would like his dictatorship to last as long as he lasts. Contrary to that, once dictatorship is no longer popular, the people no longer wish to see it. Some compromise is possible as long as the dictatorship does not rely on force alone. As long as it can guarantee some economic or political benefits, it can compensate the people for the coercion they have to accept. However, immediately after it is left with coercion only, the dictatorship has to fight for its survival almost daily even if it controls everything that can be controlled. The end of such a regime becomes the only political issue in the country. This is the current situation in Serbia.

The key problem of the dictatorship in Serbia is that it cannot become anything else. The regime may at some point in the near future decide to call elections, which it cannot afford to lose, so it will win them. But, that will not change much. It will solve a problem or two, which were downgraded to almost pure technical ones, with the use of violence and coercion. But this will not make economic and political instruments available. Thus, force will still have to be used practically all the time.

There is one remaining issue. How long can it use force efficiently? The answer depends on many things. However, once the opposition parties are marginalized, and that process has practically been completed, the regime will have to face new resistance. How it will deal with it is yet to be seen, but the consequences will be even worse than those in the last decade or so. The theory of dictatorships claims that there is an advantage of centralized dictatorships over decentralized ones. The experience of former Yugoslavia is atypical in that respect. The same will happen to Serbia. If it cannot change, it will disintegrate. People will start looking for protection locally, as they cannot get it nationally. Given the international environment of Serbia, this is practically inevitable. Thus, the success of dictatorship in Serbia, if it comes, will be at the expense of a national breakup. This has already been a distinctive accomplishment of the current regime, only now it is closer than ever.

# analysis:

## Fruit Production in Serbia

*Ivana Dulić Marković*

Fruit production in the contemporary world develops through the concept of integral production, which presumes the economical production of high quality goods where priority is given to the ecologically safest methods. In the fields of agrology and pomology significant results were obtained with all fruit cultures that give production all the traits of intensive utilization of cultivation technology, with a high degree of production space utilization. The result of which is production growth alongside a reduction of fruit planted areas, an increase of production efficiency and fruit quality, and the solution of important issues that concern the preservation of living environment.

All agro-economic research clearly shows that agriculture development depends upon new technologies based on knowledge, in industrial and developing countries alike. Knowledge has become the main, often the most lucrative factor in the development of agriculture. Fruit production has large accumulateness: apples are 35.2 times more cumulative than wheat, 15.7 times more than corn, and 7.36 times more than potatoes. However, it also requires a high degree of expertise, which gives production all the attributes of a specialist production of commodities.

### ***Deep crisis of fruit production***

Fruit production is in a deep crisis in Yugoslavia, with little prospects for recovery in the near term. Current fruit production in Yugoslavia demonstrates great differences in the level of intensiveness depending on the area of cultivation. The degree of fruit growing development is especially hampered in traditional fruit growing regions, where the applied agrology and pomology measures have all the characteristics of semi-intensive production with a small degree of production capacity utilization.

In recent years, individual production on farms, which is diverse in structure, has been left unprotected due to the disappearance or deterioration of collective farms and other production organizers, and subject to severe blows on the market of raw materials, as well as that of final products – which led to still larger extensiveness of production and rapid deterioration of long-standing plantations.

Plum production (40,000 wagons) is based on a large number of trees with small yield, while 75% of production goes into plum brandy. Apple production (20,000 wagons) can hardly reach competitive levels on the world market even after a lifting of sanctions, while the domestic market is too small for ambitious development. Only raspberries have become a product of national and strategic importance for the Yugoslav economy (45,000 t, 60 million USD), however in the last few years disrupted economic ties between primary production and processing, and the neglect of primary production and quality of merchandise have opened space for competition (Chile, Spain, Poland) to replace Yugoslavia as the leading producer of raspberries on the world market.

### ***A modest but "safe" sort***

The contemporary concept of intensifying fruit production gives optimal results when three conditions are observed: sort/foundation, orchard system, and ecological conditions in the place of cultivation. Growing requirements of the market impose swift changes of assortment and the introduction of new sorts and clones into production. In the EU assortment of apples the dominant sorts are Golden Delicious with 37.17%, Red Delicious with 11.32%, Jonagold with 9.42%, Granny Smith with 5.25. The expansion of sorts such as Jonagold, Elstar, Gala, Breburn and Fuji, as well as their mutants and clones, is evident. Characteristic of our country is widespread and increasing use of the Eidared sort, which is priced as industrial fruit on the European market (0.19 DEM) – as opposed to other sorts (Breburn 0.85 DEM, Gala 0.80 DEM, Golden Delicious – from hilly terrain 0.58 DEM, Red Delicious 0.58 DEM, Golden Delicious – from plains 0.38 DEM, Gloucester 0.23

***Knowledge is the  
most lucrative factor  
of agriculture***

***Even after borders  
open FRY will not be  
competitive***

***The "safest" sorts are  
those which  
withstand ignorance***

DEM). This apple sort, of very modest quality, is in our country considered as one of the "safest" sorts with regard to regularity and abundance of crop. Denoting that it is grown only because it "withstands ignorance" – whatever scientific agricultural and fruit growing measures are applied, it bears well.

Current sorts and their clones that are in demand on the European market (Gala, Breburn, Fuji) are grown only as individual attempts on specialized fruit farms, usually on intensive plantations close to large consumer centers (Smederevo, Grocka, Novi Sad, Subotica).

Early plum sorts are very much in demand and very profitable. Until August 1st each year, 9,000 wagons of Table Plum at 1.2 – 1.5 DEM/kg are exported from northern Italy to Germany. Among other exported sorts is the *\_a\_ak Beauty* (*\_a\_anska lepotica*), created at the Center for Fruit Growing in *\_a\_ak* but grown in Italy, by using the spindle-like cultivation pattern and orchards of the "arm length" type. The *\_a\_ak Beauty* planted at 3.8 x 0.8 distances (3,280 saplings/ha) gives 86 – 117 fruits per tree in as early as the second year. With the average fruit body mass of 41.5 g, each tree gives 4.21 kg or 1.38 wagons/ha of high-class fruit. In full fruitage a yield of 4 – 4.9 wagons/ha is reached.

### No program for sapling production

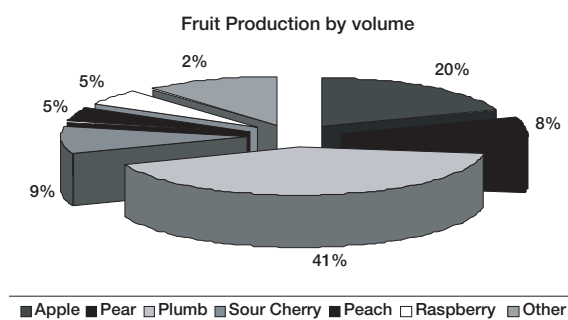
Errors that are made when an orchard is raised remain as long as the orchard lasts, so that the production of saplings, i.e. non-viral seedling material, is a very important aspect of the improvement of fruit growing. Non-viral seedlings result from a program consisting of the production, maintenance, reproduction and distribution of plant material, aiming to sell it with an official certificate that guarantees a certain category. The goal of producing seedlings is to provide standardized plants for fruit producers that are free of pathogens, high in quality and of a certified sort. Responsibility in seedling production should be contained in the declaration, or label that accompanies the seedling.

Production programs for non-viral seedlings (certification programs) differ depending on the fruit that is bred, the goals and purpose of the program, equipment, finances, expertise, and the importance of the viral disease problem for the yield of a certain fruit. All programs of certification are managed on the national level, by the government and through the Ministry of Agriculture.

Uncontrolled sale of seedlings in Yugoslavia led to dramatic consequences, like the endangered production of drupaceous fruits due to the spreading of plum pox potyvirus disease, the *erwinia amylovora* on pomaceous fruits, and the widespread withering of raspberries caused by fungus from the *verticillium* family.

The importance of contriving such programs as soon as possible is best illustrated by this year's import of raspberry seedlings. In the course of spring 2000, Yugoslavia imported 90,000 – 100,000 seedlings of the vilamet sort (at 1.2 DEM), and 70,000 of the miker sort (at 1.5 DEM) that were paid over 220,000 DEM. This quantity of seedlings can be produced very easily on a 1 ha large breeding farm!

**Imported raspberry seedlings could have been produced on 1ha**



### "Arm length" orchards

The current situation in fruit growing, above all the issue of intensifying through high productivity (the price drop of apples and pears on the international market in recent years is above all a consequence of productivity increases achieved by contemporary methods of "arm length" cultivation), high quality of fruit relative to the amount of yield and the ability to store under controlled conditions, and quick changes of assortment impose the problem of an overall evaluation of orchards, given that substantial financial means are at stake. In Yugoslavia, goals have to be set in the sense of attaining contemporary systems based on adequate application of knowledge, and quick acceptance and change of assortments that are in demand on the world market.

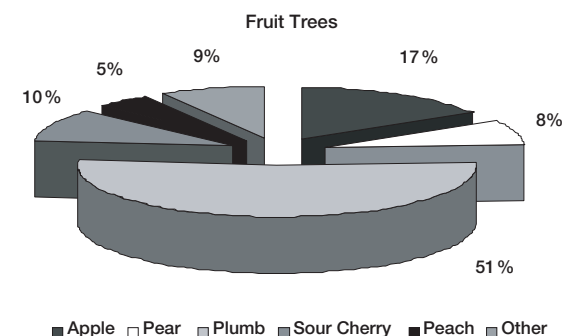
Basic factors in defining contemporary systems are those that determine economic success. All contemporary systems of fruit cultivation are based on the same concept, which is defined by the following principles:

1. low plantations – the height of the habitus is kept on the level where all interventions on trees can be accomplished from ground level – "plantations at arm length"

2. optimal pattern density – the number of trees per unit increases to obtain maximum use of production space

3. control of tree formation and replacement – specific genotype characteristics are respected in applying pomological interventions to different systems of cultivation.

A discussion on differences in contemporary cultivation systems' efficiency would require the analysis of total costs, beginning with initial investment and interest rates, to the total cost of maintenance and marketing of obtained crop, i.e. obtained profit.



1. Mićić, N. & ass., Achievements and Contemporary Tendencies in Agrology and Pomology of Fruits, Jugosl. Vocar., 117-118; 135-151, 1997.

2. Blaser et al., Analyse comparative des performances économiques de différents systèmes de verger, Revue Suisse Vitic. Arboric Hortic., vol.28: 117-128, 1996.



## Beginning again in the early 1970's

In that sense, the study of different aspects of fruit growing systems by Blaser and his associates is especially interesting. They analyzed orchard systems with the following cultivation patterns: palmate (3.5 x 2.5 m), slim spindle (4.0 x 1.5 m), four-axes spindle (3.8 x 1.5 m), "V" planted spindle (3.5 x 0.9 m), Solen – "bent spindle" (3.8 x 1.5 m), and super-spindle (3.0 x 1.0 x 0.5 m) with the Golden Delicious sort on M9 foundation. Differences in productivity of these systems show high output of the super-spindle, larger output of "V" planting as compared to other spindle systems, and lowest output of the palmate system.

The analysis of economic indexes during the whole exploitation period, however, gives a totally different picture. Namely, agronomic and economic analyses of the six orchard systems demonstrate the following: the palmate system, despite low cultivation costs, is deficient because of the small number of trees/ha, subsequent thinning of orchards and the overall negative balance.

On the contrary, the super-spindle system, which is very intensive and gives early crop, is economically justified only if the price of first class apples exceeds 1.60 DEM/kg because of high cultivation costs (10,000 saplings/ha) and the need for trained labor. This is too high a price, but when the system is applied to standard sorts it also shows a negative balance. The Solen – "bent spindle" and "V" planting systems obtain the greatest liquidity.

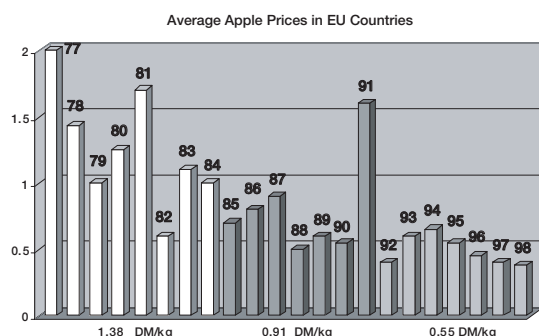
The difference between analyzed systems, viewed through profit obtained at the end of the exploitation period (total profit – total cost) and modeled by Arboflux software, shows that the greatest accumulation, compared to the slim spindle as standard, was achieved by: Solen – "bent spindle" (8x), "V" planting (7x), and four-axes spindle (2x), while the super-spindle (-3x) and palmate (-4x) gave a negative balance.

Although these results were obtained under Swiss market conditions (differences in product price, seasonal and qualified labor prices) they can be very indicative with relation to gross product and costs of specific labor operations, and serve as a basis for defining development programs for the improvement of fruit growing in our country. In Yugoslavia, analysis of applied agrology and pomology measures and the structure of cultivation patterns clearly show that we are at the beginning of the 1970's.

In that period, Europe started to abandon the palmate system and introduce the spindle as a cultivation pattern standard. Today Europe uses two and three-axes spindles and the bent spindle (Solen), and modifications of spindles that allow a density of 5 – 6000 saplings/ha. In northern Italy, the density of apple trees in the slim spindle pattern falls between 2.500 – 3.350 (3,2 – 3,6 x 1,0 – 1,2 m) and 3.940 – 5.100 (2,8 – 3,2 x 0,7 – 0,8 m), depending on the sort.

If only one argument could be found to mitigate our conclusion that fruit production in our country is over-extensive, then it would be the fact that we do not have to waste time in seeking out

the most productive cultivation systems to reach intensiveness, instead we can apply experience acquired in developed countries that is modified to our production conditions.



## Area instead of trees

The contemporary concept of orchard systems contains a different view on the crop issue. While classical cultivation systems considered the yield per tree as their basic concern and issue, today the yield is perceived by unit of cultivated area and expressed in kg/m<sup>2</sup>. This concept is

based on the following elements: all agronomy measures are performed by unit of cultivated area (cultivation, fertilizing, etc.), so the cost is accounted correspondingly; the degree of productive space utilization is in direct relation with production output; the total scope of production is much more important than yield per individual tree.

Accordingly, for example, if an area of 3.8 x 2.0 m is planted instead of an area of 3.8 x 1.5 m, losses per one hectare are as follows: the unproductive area is 2,498.5 m<sup>2</sup>, idle speed of the tractor is (1 stretching) 657.5 m, atomizer work for 10 sprayings during vegetation is 6.57 km, total machine functioning in empty space 11.83 km, which all reflect in an amount of 5,625 kg of yield loss.

Intensive development of fruit growing in the last years imposed a standard of 5-6 wagons per hectare of extra quality apples. Only producers that can accomplish this are considered as market competitive. In order to satisfy demands of like production, only ramified saplings are planted in order to obtain a yield of 22 fruits or 5 kg per tree, or 1.25 – 1.55 w/ha in the second year of cultivation. In the third year, the amount of fruits per tree rises to 63.12 kg, or 3 – 4.1 w/ha. From the fourth year onwards, yield is established at 5 – 6 wagons per hectare.

In Yugoslavia, orchards with pyramidal cultivation form of 5 x 4 m and 4 x 4 m planting pattern give maximum yield of 2.00 – 2.50 w/ha, 50% of which is first class fruit. Yield in the palmate pattern (4 x 3 m) reach the level of 2.5 – 3.5 w/ha, while the slant-branch palmate pattern gives 70-80 % of first class fruit. Spindle-like forms achieve yields of 4 –5 w/ha and 80-90% of first class fruit.

Apart from improving production technology, it would be necessary to:

1. protect fruit such as raspberry and plum as products of national importance, like it is done in developed market economies,
2. reaffirm good production models like the model from the town of Arilje for raspberry production in the 1980's, with regard to organization, cultivation and sale of raspberries in correlation with ongoing changes of social and economic circumstances in the country,
3. organize fruit growers into an Association that would decide upon significant issues and regulations on fruit growing, and thus protect production from politics and political changes (French producers and processors of plum established the French Plum Board with a budget of 4.6 million USD for 1999/2000; over half the amount is assigned to marketing activities, while the rest is spent on research and technical activities),
4. fruit should be approached in a less idealized fashion and more as an "object of work."

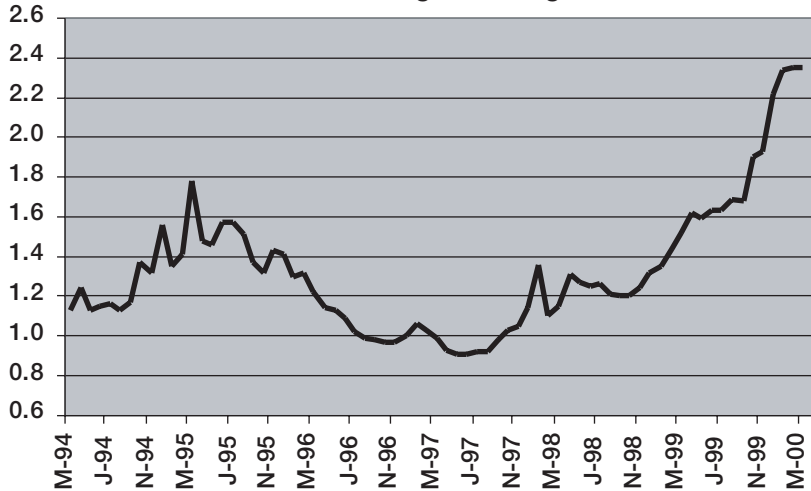
**Production in Serbia  
is based on trees  
rather than  
plantation area**

**The French Plum  
Board disposes of a  
4.6 mil USD budget**

# Macroeconomic Review

*Faced with possible expenses, the Federal Government and National Bank of Yugoslavia have given up on official devaluation and decided upon selective foreign currency restrictions. - The existing multiple foreign exchange rate system is enriched by a new - stimulative rate. - Expansive monetary policy in May? - Industrial production in the first four months is greater by 3.4 % in comparison to the previous year. Opening of borders to Montenegro.*

Real Foreign Exchange Rate



## Foreign trade and foreign exchange rate

The most turbulent event that took place in the previous month concerned the exchange rate and measures taken by certain Federal organs. As mentioned in previous issues of the Economic Review, high monthly levels of foreign trade deficit initiated the issue of its financing in the following period. In the first quarter of this year Serbia's export reached the amount of 449 million dollars, while imports amounted to 1,110 million dollars. At this pace, the deficit in foreign trade could reach the very high level of over 16% of the GDP.

The existing system relied on a series of trade and foreign currency restrictions. As the official foreign currency rate was used for accounting, the thus deformed system could exist only until the parallel rate did not significantly deviate from the official one. Cheap import stimulated the purchase of consumer goods in such a way that in the first four months their share in entire import was as high as 47%. The lack of foreign currency and the way it was being spent imposed the need for the federal government to react through the Federal Customs Administration (FCA). Following an internal directory from the FCA, a new foreign exchange rate of 19 dinars to 1 DEM was applied.

Did devaluation take place at that point?

Formally – no. The Federal Government can enact a devaluation, upon a proposal from the National Bank, but no word came through. Essentially – it did. The basic function of the official foreign exchange rate, out of the few that remain, would have ceased. The existing deformed system was at that moment completely inconsistent with devaluation. As the initial measure made imports of all goods linearly more expensive, the new, high customs' rates would have led to a rapid spreading of inflation.

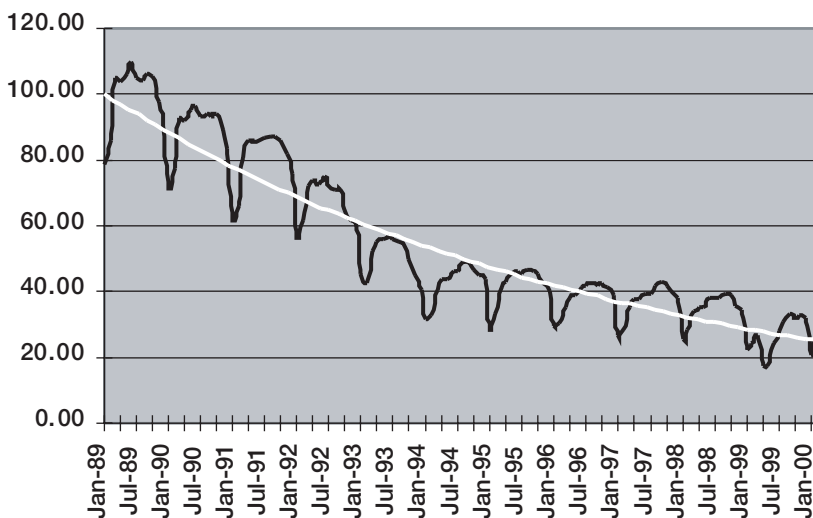
Assessment of the cost-benefit relation as dependent upon such a decision resulted in a swift new solution.

This time with the introduction of a tax by which consumer goods, cars and oil derivatives were selectively burdened. Besides the existing multiple exchange rate system another one was added. It is the so called "stimulative rate" (20 dinars to 1 DEM) which will be applied, among other purposes, to the obligatory sale of a share of foreign currency revenue by exporters and the purchase of foreign currency from citizens.

The justification of this decision cites two goals - activation of a consistent foreign currency market and stimulation of exports. The first goal will most certainly not be accomplished. This market, as anticipated, has not been functioning in the past few years. Foreign currency income will somewhat increase, since exporters will bear losses to a small degree as a consequence of the difference in exchange rates during obligatory foreign currency sale, so that a small portion will return to legal channels. In any case, loss from the sale of foreign currency does exist, and therefore it cannot be stimulating.

The second goal needs a more detailed explanation. The chart shows the real black market foreign exchange rate, expressed in dinars with steady purchasing power from March 1994, achieved by deflating the black market rate by the retail price index. Since exporters sell their foreign currency income at this rate, let us assume that it describes the competitiveness of Serbian exports well enough. Even though the real rate is more favorable as compared to the previous period,

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numerous export restrictions represent the key determinants of Yugoslav exports. The possible argument that cheap import of raw materials is thus enabled is not an adequate formulation, since it was the same in the previous period. The previous analysis imposes a simple conclusion that balance-of-payment restrictions will be an obstacle in achieving higher growth rates.

What consequences will result from the measures? The redirection of demand will be short-lived and will directly depend on stability of the parallel foreign currency market. The inflationary effect will be incomparably smaller with regard to the initial, ineptly taken decision. The non-transparent system will be even more vague, while the motive for avoiding high customs' obligations will be higher, leading to an increase of corruption since interest groups will request exemption from this decision. The way in which the decision will be carried out brings another uncertainty into future decisions of the government. Due to an exceptional presence of price control and escalation of distortion in domestic and foreign prices, additional pressure from domestic producers will occur. A partial reduction of price control would give a chance for domestic products to come under the price umbrella of imported goods, but whether that will happen depends on the pressure and shifting of price control into new

sectors. Due to a fall of real income, one of the objectives was to fill the federal budget – by contributing to the strengthening of state finances from which defense and security functions are serviced, as well as the social function of the state. The state will take a piece of the pie due to relatively rigid import, but it will have to agree to inflationary pressures based on higher prices of imported goods. This effect also vanishes with the decrease of real burdening of imports. In the long run, which is a period of a couple of months in the Yugoslav economy, pressures will be hard to resist, especially under conditions of inconsistent implementation of other policies.

## Monetary policy

At the end of April, nominal money supply amounted to 17.8 billion dinars, which is an insignificant increase as compared to the end of March (+0.8%). At the same time, the declining tendency of the real money supply continued (666 billion DEM), which adds to the image of deep depression in the Serbian economy.

During the first twenty days of May, the National Bank issued up to a billion dinars and hence increased the money supply to 18.8 billion dinars. The sudden monetary expansion did not influence growth of the black market exchange rate due to two reasons. First, the street rate remained unchanged due to the change in monetary supply structure – the amount of cash in circulation was diminished by around 600 billion dinars, which reduced the money supply on the street, while money deposits increased by 1.6 billion dinars. Second, the increase of money deposits did not immediately have an effect on growth of the pegged exchange rate, since the state significantly increased real import taxes that blocked import in the short term and at the same time reduced the industry's demand for foreign currency. Simultaneously, a significant part of the enlarged money deposits was hoarded in the form of so-called central deposits in the National Bank, thus its effect on exchange rate growth was temporarily alleviated. However, it is certain that when the state makes first significant cash payments (wages, pensions, old foreign currency savings), and after the economy adjusts to the new import regime, the street rate and the pegged rate will considerably increase, which will influence a significant acceleration of inflation.

It was announced that old foreign currency savings could be withdrawn before due time and that the new exchange rate of 20 dinars will be applied. Considering that the date of regular payment is close, clients would probably wait a few more days and renounce from the previous opportunity. Nevertheless, any announcement on an extension of the time limit would, due to previous very bad experience, produce long cues in banks very fast, since the majority would accept to pay (now a relatively small) negative exchange rate difference as the price for risk aversion. According to the new exchange rate total duties, expressed in dinars, are three billion dinars or 1/6 of the existing money mass. The settling of duties by relying on these means only would cause an extreme expansion of money mass, hence the fulfillment of duties will probably have mixed character – using different variations of settling foreign savings.

## Industry

A seasonal drop of industrial production occurred in April. Compared to the previous month it was down by 10.9%. In Montenegro production is down by 8.2%, and in Serbia by 11.0%. Production grew only in seven industrial branches, where the largest growth was registered in the production and processing of tobacco (+32.9%). Nevertheless, we get a different interpretation of the existing situation by analyzing the de-seasoned index. It shows growth in comparison to March by 2.2%, which means that previous data on the fall of production in April show only a nominal drop – because of more non-working days.

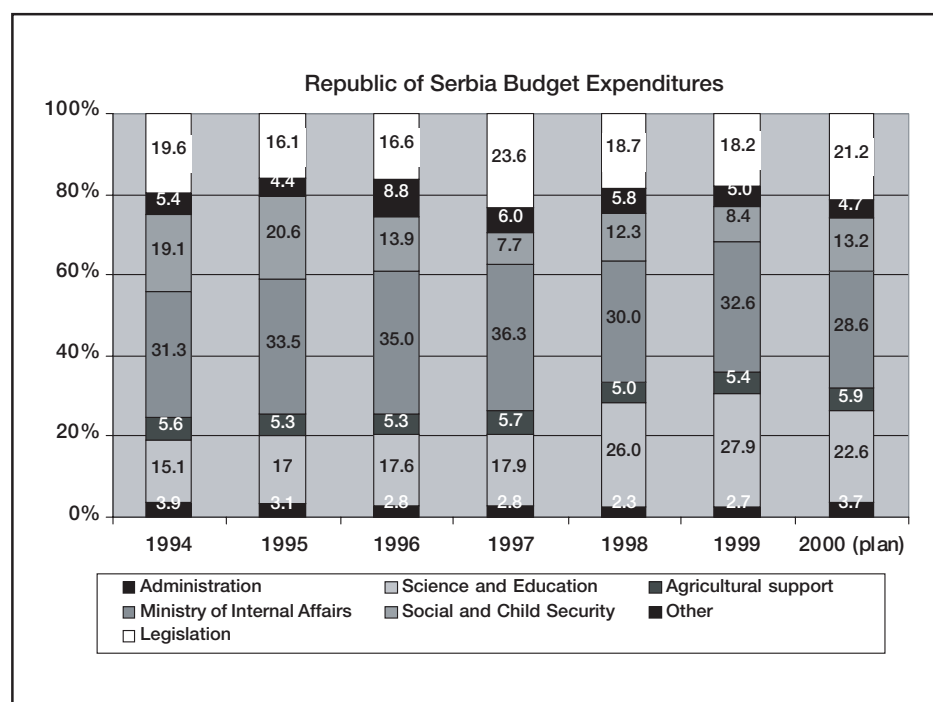
Compared to the previous year, industrial production in Yugoslavia rose by 3.4 % in the first four months of the year 2000. Taking into account a very low base, one cannot say that we are talking about a very high rate. An interesting fact is that production in central Serbia increased by 7.9 %, while in Vojvodina it decreased by 4.3 %. Industrial production in Yugoslavia was down by 71.3 % in April 2000 in comparison to April 1989, and in the period January-April 2000, as compared to the same in 1989, it was down by 69.8%.

Because of recent statements on the construction of 10,000 apartments, we made a chart to show how many apartment were built in the past and at which rate the number of finished apartments declined from year to year. Will the declining tendency stop, as announced, and show a "sudden rise", when it is evident that the rate of 50,000 finished apartments a year was a usual occurrence in the 1980s?

## Prices and salaries

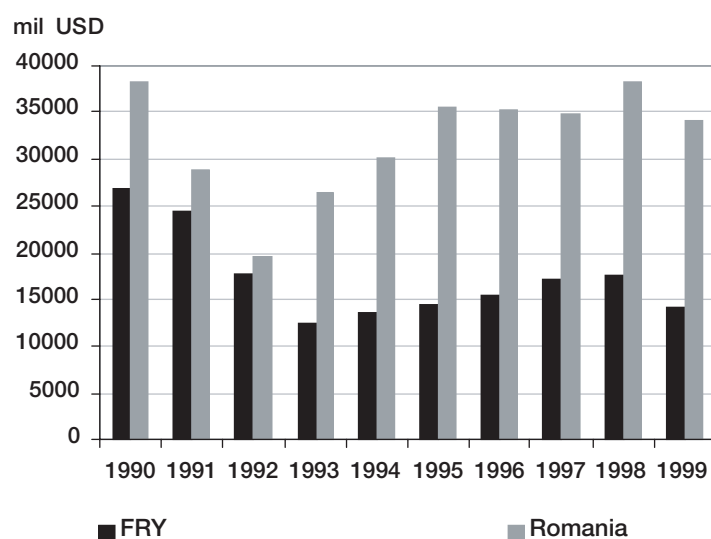
Facts presenting monthly inflation rates should be taken with reserve due to reasons mentioned in the previous issue of the Economic Review. According to Official Statements of the Federal Statistics Bureau, the monthly inflation rate in Serbia in April was 3.5%, which is an increase of 8.2% as compared to December 1999. Measured by living expenses, the monthly growth of prices is 3.3%, up 9.2% compared to the end of the previous year. Tobacco and drinks marked the largest increase at 11.6% due to the increase of retail prices by 26%. Food prices show a growth of 3.3%, in spite of the fall in agricultural products' retail prices and the small increase of industrial food prices. The announcement of poor yields and a respective decrease of supply will increase prices on the green market.

Average salaries expressed in DEM are 88 in Serbia and 154 DEM in Montenegro. Even though salaries increased in Montenegro, real purchase power is lower due to a higher inflation rate. It will be interesting to observe the effects of an opening of borders between Serbia and Montenegro on prices in the latter. There are two reasons for suspending the embargo. The first one is political and related to local elections in two Montenegrin municipalities; the other is related to the need for increased "export" from Serbia and has an economic character. If the blockade suspension will be long or short-lived depends, unfortunately, on results related to the first reason.

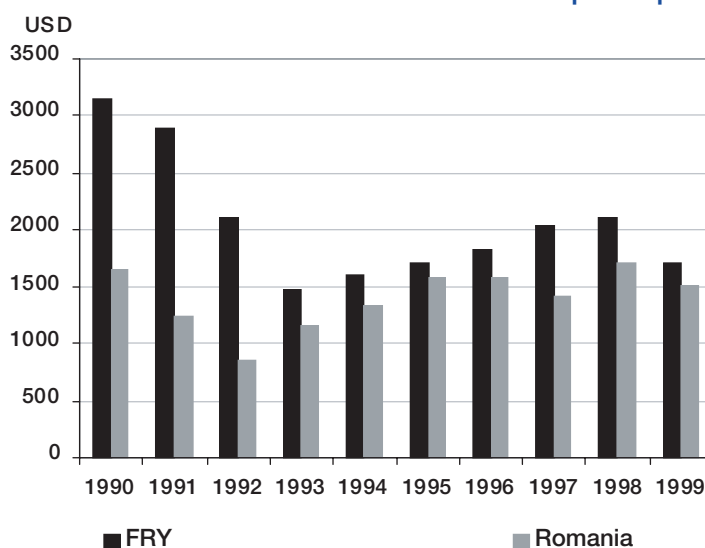


# Yugoslavia in the mirror of Eastern Europe

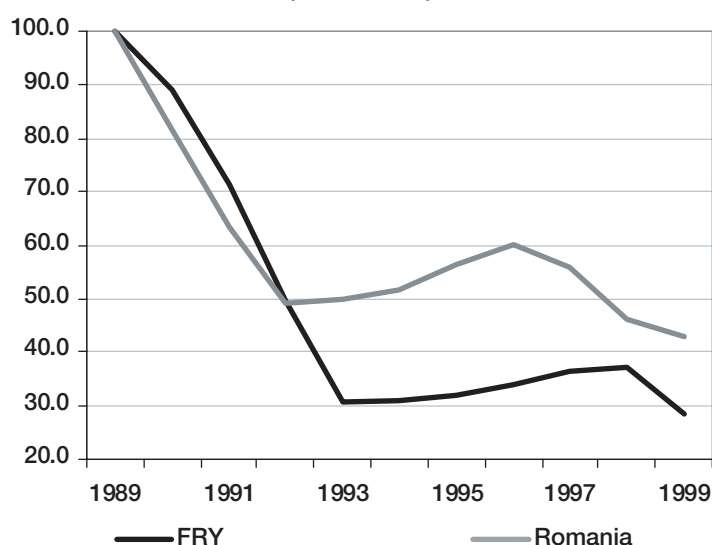
## GDP



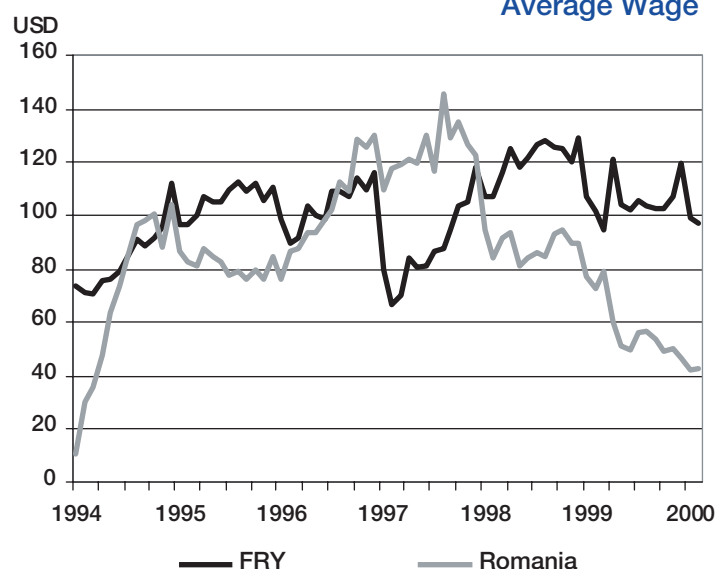
## GDP per capita



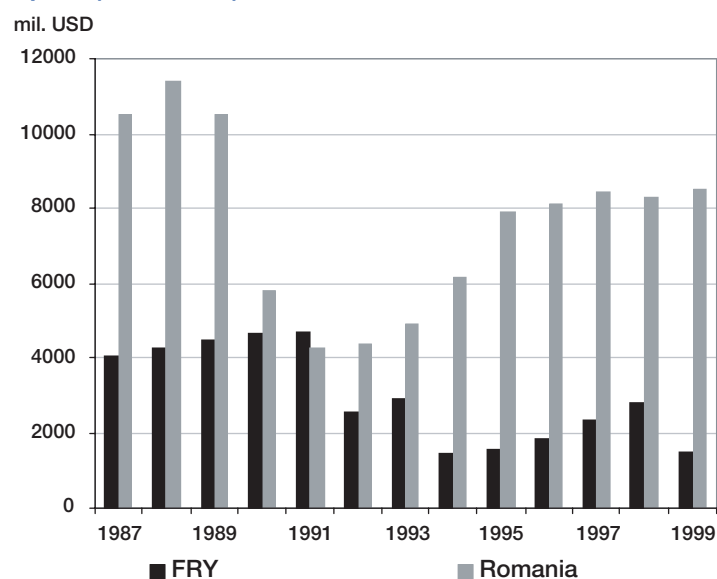
## Industrial Production (1989=100)



## Average Wage



## Import (1990=100)



## Export (1990=100)

